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R.I. banks on selling 'war' bonds

The state hopes residents and small investors will buy tax anticipation bonds to help it pay its bills.

BY STEVE PEOPLES

JOURNAL STATE HOUSE BUREAU

PROVIDENCE — Government leaders are turning to the citizens of Rhode Island to help avert a financial disaster, according to an

days by selling short-term bonds to residents, small businesses and financial institutions.

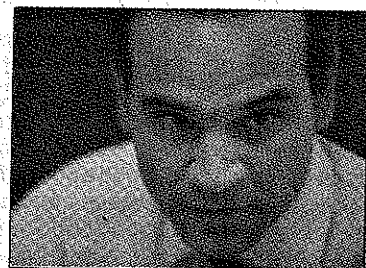
Issuing a call to duty reminiscent of the federal government's sale of war bonds nearly a century ago, General Treasurer Frank T. Caprio said the state would have trouble paying its bills in "about a month" without the sale of the bonds, known as tax anticipation notes. Recent financial instability across the globe suggests that the market for such notes is tenuous at best, especially among larger institutions that

typically purchase state and municipal bonds.

That's why state leaders have taken the unprecedented move of opening the bond sale — set for Monday, pending market conditions — to average citizens.

"Rhode Islanders have a strong tradition of responding in times of need, whether it's a natural disaster, a snowstorm, defending our country," Caprio said. "We're in a financial crisis that some are calling a once-in-a-century sequence of events. And this is one where Rhode Islanders can step up and assist the state at this time."

The sale of tax anticipation



JOURNAL FILES/ CONNIE GROSCH

Rhode Island General Treasurer Frank Caprio talks about the state's finances.

notes by the state is not unprecedented.

State leaders have authorized

such borrowing in each of the last three years, including this one. They also relied heavily on the

tactic during the credit union crisis of the early 1990s. The current state budget authorizes the state to borrow up to \$350 million, the highest amount in state history.

But never before has Rhode Island encouraged, if not depended upon, citizens to play a role.

State leaders have arranged for Bank of America branches in Newport, Providence, Barrington, Cranston, Woonsocket and Westerly to sell the notes on Monday. Investors don't need to be Bank of America customers. Citizens may also invest through their brokers, or by calling a toll-free number.

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The deal will operate largely like an eight-month certificate of deposit, or CD. For a minimum investment of \$1,000, the state will offer an interest rate "in the 3 percent range" (the actual rate will be set by the market Monday).

The interest earned is tax free for Rhode Island and federal tax filers; the notes will be repaid June 30, 2009.

Caprio expects to sell notes worth \$350 million on Monday alone, though the sale could be extended until Tuesday. He admits that the window in which the state could successfully sell such bonds in today's volatile marketplace is extremely small.

"We're optimistic that there's going to be strong demand for this," Caprio said. "The market ... has opened in our favor Wednesday and Thursday. We feel we need to get to the market now before there are any changes. It's changing by the hour."

Caprio, who crafted the plan, said he would have liked to mount an advertising campaign encouraging citizens to buy the bonds, much the same way California officials did earlier in the month when they raised \$5 billion to avert a cash shortage.

California was forced to rely upon individual investors to help sell its tax anticipation notes, largely because the national credit crisis scared off the Wall Street firms, hedge funds and other institutions that typically drive the bond market, according to a recent Bloomberg report. Massachusetts earlier in the month raised \$750 million much the same way, but only after volatility in credit markets forced state officials to delay its sale by a week.

Governor Carcieri issued a letter earlier in the month allowing the sale of the tax anticipation notes. He did not address the issue publicly yesterday, but his spokeswoman Amy Kempe played down the significance of the move.

"It's one of the tools in the arsenal that the state has," she said. "It's something the state has done before to manage its cash flow."

Indeed, since 1991, Rhode Island has relied on tax anticipation notes to help pay its bills six times when economic conditions slowed the receipt of revenue the state needs to function, according to data released by the treasurer's office.

While the state had never borrowed as much as \$350 million, it borrowed a higher percentage of its previous year's

tax returns — a standard used to measure tax anticipation notes — in 1991 (\$200 million), 1992 (\$240 million) and 1993 (\$225 million).

This year, the state had planned to wait until early December to sell the notes, according to Caprio. But it was driven by market conditions and a shortage of cash to act now.

"In about a month, we would have to start making decisions as to which items would be paid and which would be put off," he said, noting that the state hasn't deferred payment on its responsibilities in nearly two decades.

Tax anticipation notes essentially give the state immediate access to tax revenue that wouldn't ordinarily flow into the state's coffers until late spring. But there's a cost associated with the maneuver.

The treasurer's office estimates the related debt will cost taxpayers \$5.3 million, which was accounted for in the state budget.

Rhode Island is no stranger to budget and economic woes. Rhode Islanders learned earlier in the week they have the highest unemployment rate in the nation, 8.8 percent.

The governor's office announced yesterday that Carcieri will convene an economic forum "to develop short- and long-term solutions to pull Rhode Island out of the recession, create jobs and stimulate economic growth." The meeting of "the state's top business and labor leaders, policymakers and academics" will be held Nov. 6.

And Carcieri suggested he may call on the state legislature to hold a special session to respond to the situation; the part-time Assembly isn't scheduled to return until January.

"We cannot wait until January to have this discussion,"

Carcieri said in a statement.

Meanwhile, Caprio said he'll monitor the financial markets closely in the coming days to determine whether to delay Monday's sale. Major events over the weekend or early Monday could change the schedule.

Absent a formal advertising campaign, Caprio said he'd depend on local media to get his message out. He will hold a news conference announcing the plan this morning.

"We're in unprecedented financial times," he said. "If an investor in Rhode Island, a family or small business, has a need to invest money for the next eight months and they're looking for a fair rate that's backed by the full faith and credit of the taxpayers of the State of Rhode Island, this investment has been made available to them in a way that it hasn't been made available in the past."

Caprio continued: "There's work that everybody can do to move Rhode Island in the right direction."

Updated information, a full list of participating Bank of America branches, and the toll-free phone number will be posted on the treasurer's Web site: www.treasury.ri.gov/

speoples@projo.com / (401) 277-7513

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